

Message Text

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ACTION EUR-12

INFO OCT-01 ISO-00 CIAE-00 DODE-00 PM-03 H-02 INR-07 L-03

NSAE-00 NSC-05 PA-01 PRS-01 SP-02 SS-15 USIA-06

AID-05 EB-07 CIEP-01 TRSE-00 STR-04 OMB-01 CEA-01

COME-00 FRB-03 XMB-02 OPIC-03 LAB-04 SIL-01 /090 W

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R 041842Z JUN 75

FM AMEMBASSY LONDON

TO SECSTATE WASHDC 1677

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E.O. 11652: N/A

TAGS: EGEN

SUBJECT: BRITAIN'S ECONOMIC FUTURE; REVELATION 6,8?

1. AN EXTREMELY DARK PICTURE OF THE FUTURE OF BRITAIN'S ECONOMY HAS BEEN PAINTED RECENTLY IN A NUMBER OF AMERICAN COLUMNS AND PUBLICATIONS, TOPPED ONLY BY THE APOCALYPTIC VISION IN FULL COLOR ON THE COVER OF THE ECONOMIST. THOUGH THERE IS A GOOD DEAL OF TRUTH IN ALL OF THESE COMMENTARIES AND THE ECONOMIC FUTURE OF BRITAIN IS INDEED RATHER DARK, THE EMBASSY BELIEVES THAT MANY OF THESE PICTURES ARE NOT BALANCED AND ARE MORE PESSIMISTIC THAN IS JUSTIFIED BY THE FACTS.

2. IT IS TRUE THAT BRITAIN HAS THE LOWEST GROWTH RATE AMONG THE OECD COUNTRIES FOR ALMOST ANY PERIOD OF RECENT YEARS ONE MAY CARE TO CONSIDER; THAT MUCH OF ITS INDUSTRY, BOTH NATIONALIZED AND PRIVATE, IS WEAK AND INEFFICIENT, MANAGEMENT AND INDUSTRIAL RELATIONS ARE POOR, PROFITS ARE LOW AND INVESTMENT IS INADEQUATE; THAT ITS CURRENT RATE OF INFLATION IS ROUGHLY DOUBLE THAT OF MOST OTHERS, AND GROWING WORSE; THAT ITS BUDGET DEFICIT IS FANTASTIC (SOME 9 TO 10 PERCENT OF GROSS

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DOMESTIC PRODUCT); THAT IT LIVES ON BORROWING, WITH

A SUBSTANTIAL BALANCE OF PAYMENTS DEFICIT; THAT LABOR IS SHORT ON DISCIPLINE AND A STRONG LEFTIST ELEMENT IS DISTURBING; AND THAT CURRENT WAGE INCREASES ARE OUT OF CONTROL AND ARE FUELING FURTHER INFLATION. CONFIDENCE IS LOW. BUT THERE ARE ALSO MORE FAVORABLE FACTORS, PARTICULARLY IN THE SHORT RUN. CONSIDER THAT INDUSTRIAL PRODUCTION AND GROSS DOMESTIC PRODUCT HAVE FALLEN OFF MUCH LESS STEEPLY THAN IN THE UNITED STATES IN 1974 AND 1975; UNEMPLOYMENT IS AT A LEVEL OF 3.6 PERCENT, ONE OF THE LOWEST IN WESTERN EUROPE AND MUCH LOWER THAN OURS; THE BALANCE OF PAYMENTS IS MUCH IMPROVED IN RECENT MONTHS; RESERVES ARE AT A HIGH LEVEL, EVEN THOUGH THEY FELL 10 PERCENT LAST MONTH; AND STOCK MARKET AVERAGES ARE AT MORE THAN TWICE THEIR JANUARY LEVEL. SOME OF THE MORE FAVORABLE SHORT RUN FACTORS, NOTABLY THE SO FAR SHALLOW RECESSION AND RELATIVELY LOW LEVEL OF UNEMPLOYMENT, PROBABLY ARE DUE TO THE FACT THAT BRITAIN IS IN A FAIRLY EARLY STAGE OF THE RECESSION CYCLE. ON THE OTHER HAND SOME OF THE BAD STATISTICS, THE FACT OF THE RECESSION AND THE BALANCE OF PAYMENTS DEFICIT, ARE PARTLY DUE TO EXTERNAL FACTORS, THE WORLD RECESSION AND THE HIGH PRICE OF OIL. SOME OF THE LONG RUN NEGATIVE FACTORS, NOTABLY LOW INVESTMENT, ARE ALSO PRESENT IN THE UNITED STATES. AND THERE IS OIL IN THE FUTURE. IN ANY EVENT, THE PICTURE IS NOT ALL DARK; IT IS MIXED.

3. ALSO WORTH NOTING IS THE RELATIVE STRENGTH OF STERLING VIS-A-VIS THE DOLLAR. PLAINLY THE MARKET IS NOT IN FACT BETTING WITH THE DOOM-SAYERS. WHEN WE ASK WHY STERLING IS AS STRONG AS IT IS IN VIEW OF THE NUMEROUS PREDICTIONS OF CATASTROPHE, MANY WELL INFORMED PEOPLE SAY THE DOLLAR IS UNDERVALUED. WE AGREE THAT IT

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AID-05 EB-07 CIEP-01 TRSE-00 STR-04 OMB-01 CEA-01

COME-00 FRB-03 XMB-02 OPIC-03 LAB-04 SIL-01 /090 W

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IS; WE EXPECT, IN FACT, A SLIDE OF STERLING, PROBABLY FOR SOME TIME TO COME. THIS IS NOT TO SAY, HOWEVER, THAT THE ECONOMY WILL GRIND TO A HALT IN THE ABSENCE OF SOME MASSIVE RESCUE OPERATION. THIS IS NOT THE PICTURE. AS INFLATION CONTINUES, BRITISH GOODS WILL NOT BE PRICED OUT OF THE MARKET PRECISELY BECAUSE THE VALUE OF STERLING WILL FALL. THE PICTURE WE SEE DOMESTICALLY IS, IN THE SHORT RUN, A DEEPENING RECESSION WITH AN UPWARD MOVEMENT IN DUE COURSE, IN THE LONGER RUN, RELATIVELY SLOW GROWTH ALONG THE LINES OF THE PAST DECADE. INTERNATIONALLY, STERLING WILL CONTINUE A DOWNWARD TREND.

4. THE DEGREE OF ALL THESE MOVEMENTS IS LIKELY TO DEPEND HEAVILY ON THE EXTENT TO WHICH WAGE INCREASES AND, THEREFORE, INFLATION CAN BE BROUGHT UNDER CONTROL. THERE IS WIDESPREAD HOPE THAT THE GOVERNMENT, STRENGTHENED BY AN AFFIRMATIVE RESULT IN THE JUNE 5 REFERENDUM ON EC MEMBERSHIP, WILL TACKLE THE SUBJECT FIRMLY IN THE SUMMER OR FALL, AND WITH AT LEAST REASONABLE SUCCESS. WE SAY "HOPE" RATHER THAN "EXPECTATION,"

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BUT THERE IS AT LEAST A REASONABLE HOPE.

5. WE DO NOT MEAN TO SUGGEST THAT ALL IS WELL. INFLATION IS MORE OR LESS OUT OF CONTROL AND THE PROSPECTS FOR EARLY REDUCTION TO A LOW LEVEL ARE NOT GOOD. THIS IS SERIOUS; IT MEANS LOWER STANDARDS OF LIVING FOR THE MANY WHO CANNOT KEEP UP. IT DOES NOT NECESSARILY MEAN THE RUIN OF THE ECONOMY. THOSE WHO ARE KEEPING AHEAD OF THE INFLATION NEVER HAD IT SO GOOD, AND WE SHOULD NOT CONFUSE A PARTLY DELIBERATE SHIFT IN INCOME DISTRIBUTION WITH ECONOMIC RUIN.

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Message Attributes

Automatic Decaptioning: X
Capture Date: 01 JAN 1994
Channel Indicators: n/a
Current Classification: UNCLASSIFIED
Concepts: ECONOMIC CONDITIONS, ECONOMIC REPORTS, ECONOMIC TRENDS
Control Number: n/a
Copy: SINGLE
Draft Date: 04 JUN 1975
Decaption Date: 01 JAN 1960
Decaption Note:
Disposition Action: RELEASED
Disposition Approved on Date:
Disposition Authority: RowellE0
Disposition Case Number: n/a
Disposition Comment: 25 YEAR REVIEW
Disposition Date: 28 MAY 2004
Disposition Event:
Disposition History: n/a
Disposition Reason:
Disposition Remarks:
Document Number: 1975LONDON08502
Document Source: CORE
Document Unique ID: 00
Drafter: n/a
Enclosure: n/a
Executive Order: N/A
Errors: N/A
Film Number: D750195-0896
From: LONDON
Handling Restrictions: n/a
Image Path:
ISecure: 1
Legacy Key: link1975/newtext/t19750682/aaaacxbn.tel
Line Count: 169
Locator: TEXT ON-LINE, ON MICROFILM
Office: ACTION EUR
Original Classification: LIMITED OFFICIAL USE
Original Handling Restrictions: n/a
Original Previous Classification: n/a
Original Previous Handling Restrictions: n/a
Page Count: 4
Previous Channel Indicators: n/a
Previous Classification: LIMITED OFFICIAL USE
Previous Handling Restrictions: n/a
Reference: n/a
Review Action: RELEASED, APPROVED
Review Authority: RowellE0
Review Comment: n/a
Review Content Flags:
Review Date: 23 JUN 2003
Review Event:
Review Exemptions: n/a
Review History: RELEASED <23 JUN 2003 by CunninFX>; APPROVED <04 NOV 2003 by RowellE0>
Review Markings:

Margaret P. Grafeld
Declassified/Released
US Department of State
EO Systematic Review
06 JUL 2006

Review Media Identifier:
Review Referrals: n/a
Review Release Date: n/a
Review Release Event: n/a
Review Transfer Date:
Review Withdrawn Fields: n/a
Secure: OPEN
Status: NATIVE
Subject: BRITAIN'S ECONOMIC FUTURE; REVELATION 6,8?
TAGS: EGEN, SOPN, ECON
To: STATE
Type: TE
Markings: Margaret P. Grafeld Declassified/Released US Department of State EO Systematic Review 06 JUL 2006